FARM CREDIT EAST, ACA

William J. Lipinski
Chief Executive Officer

February 10, 2015

Mr. Barry Mardock
Deputy Director, Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, Virginia 22102-5090

Dear Mr. Mardock:

On behalf of Farm Credit East I am submitting comments on the Farm Credit Administration's (FCA or Agency) proposed capital rule.

Farm Credit East serves farmers, commercial fishermen, forest products operations, farm related businesses and eligible processing and marketing entities in a seven-state area in the Northeast which includes the States of New York, New Jersey, Connecticut, Massachusetts, Maine, New Hampshire and Rhode Island. As the largest lender to agriculture in the Northeast, our customers rely on us to serve their needs through all agricultural economic cycles. Without question, maintaining strong capital levels to meet the future growth of our customers and to successfully serve customers during down economic cycles is necessary and an integral part of our value-proposition to Northeast agriculture.

Farm Credit East (FCE) actively participates in the policy considerations of the Farm Credit Council (FCC) and fully endorses the positions expressed in their letter on these regulations. As such, it is not my intent to repeat the views expressed by FCC. In addition many members of the Farm Credit East Board of Directors have previously submitted letters which we support.

FCE appreciates the opportunity to comment on the FCA's proposed regulations on capital. FCA modernization of the capital requirements could be helpful to investors and others who are acquainted with the Basel III framework and understand the overall financial strength and capital capacity of individual Farm Credit System (FCS) institutions as cooperative financial institutions.

While we agree with the need for FCA's modernization, we have concerns that the proposed rules fail to recognize current capitalization strategies employed and the progress made by Farm Credit institutions since the agricultural crisis in the 1980's. Moreover, the proposal does not recognize institutions boards' fiduciary responsibility to safeguard an institutions capital and are a harsher approach than that being implemented by other U.S. financial regulators.

FCS institutions have successfully moved away from a system of capitalization where borrower stock with an implied guaranty of return upon loan payment was prevalent, to one where earnings are the primary source of risk based capital formation. The accumulation of capital through earnings whether those earnings are allocated to members or not is the institutions boards responsibility to control. There should not be artificial restrictions and discriminatory categorization based on the type of equity retained. Nor should there be a minimum holding period required in order to qualify capital for the tier perceived as the highest quality of capital. Commercial banks have no such requirement and there is no basis for this discrimination in the Basel III framework.

Farm Credit East has spent the last 20 years developing a cooperative model designed to deliver the highest possible value to members in the marketplace we serve. The fact that any portion of our undistributed earnings might be in the form of allocated equities does not diminish the quality of that equity retained. The board is required to approve any distributions, and the Farm Credit Administration as regulator has established the minimum capital thresholds that need to be maintained. To penalize the recognition of capital retained based on a holding period of ten years would render the current method of delivering patron value irrelevant and likely result in a model where a lower level of earnings are generated in total. In essence, this reduces the financial flexibility of institutions to deal with longer term variations of lending conditions within the chartered territory. The proposed rule for CET 1 equity also fails to recognize the success FC institutions have had managing through periods when patronage or equity revolvement has been suspended in favor of additional capital formation and retention.

We believe all retained equity should qualify for CET 1 without regard to any minimum holding period. We also believe FCA could simplify their approach with regard to approval needed for equity distribution and require FCA prior approval of any distribution if the resulting distribution would cause an institution to fall below the minimum threshold established by regulation. The proposed rule fails to recognize that any individual institution could be more than adequately capitalized even if a distribution in excess of the prior year's net income was made.

In addition we note the following concerns:

- High Volatility Commercial Real Estate (HVCRE): We support the System response asking for clarification as to what is included in this asset category that would receive a 150 percent risk weighting. The proposed regulation is silent on what is included and only specifically excludes 1-4 family residential property and agricultural transactions where real estate is at "ag only" value. In our market, most if not all of our agricultural land transactions have non-agricultural influences on the value of collateral. It would be irresponsible for FCA to implement rules containing this category of Risk Adjusted Assets without a clear understanding by institutions affected by this new concept. A clear definition of what is HVCRE will be needed before any final rules are put in place. Since we are unable at this time to identify what assets would be impacted by this asset category, additional comment periods may be needed if this approach is to move forward. We oppose any regulation that would include agricultural land whose value is affected by nonagricultural influences in the HVCRE (150 percent RW) category. This would have significant impact on our ability to lend to agriculture in our market.

- Cap on how much of the Allowance for Credit Losses (ACL) can be included in Tier 2 capital: The 1.25 percent limit on how much of the ACL can be counted in Tier 2 regulatory capital is arbitrary, and we strongly oppose this provision. The need to have ACL changes over time based on the risk characteristics of our portfolio. If our metrics indicate the need for a higher Allowance, it is counter intuitive for regulations to cap what we can include in this important component of risk capital.

- Bylaw Amendments: We do not see the need to "hard code" treatment of cooperative equities into our Bylaws when we already have well developed internal and external capitalization standards. Rather than direct capitalization bylaw changes, the FCA should rely on board policies, directives, and capital plans. Board directives are sufficient to implement FCA's proposed Basel III framework.

Thank you for the opportunity to comment on this proposed rule. Given the importance and implications of this regulation, I urge FCA to reconsider this rule and re-propose revisions for comment.

Sincerely,

William J. Lipinski
Chief Executive Officer